

Message Text

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FM AMEMBASSY ADDIS ABABA

TO SECSTATE WASHDC 7036

INFO AMEMBASSY LONDON

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TAGS: ECON EFIN

SUBJECT: EPMG BUDGETS FOR FY 1968 (ETHIOPIAN FISCAL YEAR)

REF: ADDIS ABABA TOAID A-99

SUMMARY. INFORMATION RECENTLY MADE AVAILABLE REGARDING GOVERNMENT REVENUES AND EXPENDITURES FOR ETHIOPIAN FISCAL YEARS 1966, 1967 AND 1968 (US FY 1974, 1975 AND 1976) PROVIDE SOME INSIGHT INTO THE PRIORITIES AND PERFORMANCE OF THE EPMG. THE CURRENT GOVERNMENT IS WILLING TO UNDERTAKE A MUCH MORE ACTIVIST ROLE IN DEVELOPMENT AND IS PREPARED TO FINANCE THIS INCREASED ROLE THROUGH HIGHER LEVELS OF DEFICIT FINANCE AND GREATER BORROWINGS FROM DONORS. SINCE THE PREVIOUS GOVERNMENT TENDED TO BE VERY CONSERVATIVE IN USING THESE TWO SOURCES OF FUNDS, THE EPMG HAS SOME LATITUDE IN EMPLOYING THESE FINANCING TECHNIQUES OVER THE NEXT FEW YEARS. THE EPMG MUST, NEVERTHELESS, EXERCISE SOME CARE AS INFLATIONARY PRESSURES COULD BECOME UNMANAGEABLE IF VERY HIGH LEVELS OF DEFICIT FINANCE CONTINUE FOR SEVERAL YEARS. THE EPMG HAS LIMITED OFFICIAL USE

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PLACED ITS HIGHEST DEVELOPMENT PRIORITY ON ECONOMIC ACTIVITIES WITH

AGRICULTURE AND ROAD CONSTRUCTION RECEIVING PARTICULAR ATTENTION. AS THE DEVELOPMENT BUDGET IS VERY AMBITIOUS COMPARED TO PREVIOUS YEARS, IT REMAINS TO BE SEEN IF BUDGETED LEVELS FOR FY 1968 CAN BE ACHIEVED. BASED ON FY 1967 PERFORMRANCE IT IS POSSIBLE THAT THE EPMG CAN ACHIEVE THESE LEVELS BUT AN EXTRAORDINARY EFFORT BY THE GOVERNMENT WILL CLEARLY BE REQUIRED. END SUMMARY.

1. THE ESSENTIAL ELEMENTS OF THE EPMG'S FY 1968 (US FY 1976) BUDGET ARE CONTAINED IN TABLES A AND B ALONG WITH FY 1966 - THE LAST "NORMAL YEAR" UNDER THE OLD REGIME - AND FY 1967. THE DATA FOR THE TABLES HAS BEEN TAKEN FROM THE MATERIAL PROVIDED TO AN IMF TEAM (RECENTLY IN COUNTRY ON ARTICLE 14 CONSULTATIONS) BY THE MINISTRY OF FINANCE. SOME FIGURES DIFFER FROM PREVIOUSLY PUBLISHED DATA.

TABLE A
BUDGET SUMMARY
(MILLIONS OF ETHIOPIAN DOLLARS-ETHIOPIAN FY)
PERCENT PERCENT
1966 1967 1968 CHANGES CHANGES
(ACTUAL) (PROV) (BUDGET) 67/66 68/67

I.TOTAL EXP-					
ENDITURES	762	1036	1341	36	29
A. RECURRENT					
(ORDINARY)	596	803	909	35	13
1.DOMESTIC	530	739	864	39	17
2.GRANTS	66	64	45	-3	-30
B. CAPITAL					
(DEVELOPMENT)	166	233	432	40	85
1.DOMESTIC	87	109	183	25	68
2.LOANS(NET)	47	92	194	96	111
3.GRANTS	32	32	55	-	72
II. TOTAL					
FINANCING	762	1036	1341		
A. ETHIOPIAN					
SOURCES	617	848	1046	37	23
1. TAXES	540	586	655	9	12
2. NON-TAX					
REVENUES	79	116	235	47	103
3. DEFICIT					

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FINANCING	-2	146	156	-	7
B. EXTERNAL					
SOURCES	145	188	295	30	57
1.LOANS(NET)	47	92	194	96	111
2.GRANTS	98	96	101	-2	5

2. THE IMPACT OF THE NEW REGIME ON GOVERNMENT EXPENDITURES IS IMMEDIATELY APPARENT FROM THE FOREGOING TABLE. AFTER YEARS OF

VERY CONSERVATIVE GOVERNMENT EXPENDITURES, THE OUTLAYS FOR FY 1967 INCREASED BY 36 PERCENT COMPARED WITH FY 1966 WHILE BUDGETED OUTLAYS FOR FY 1968 ARE SLATED TO INCREASE BY 29 PERCENT COMPARED WITH FY 1967. THE RATE OF INCREASE IN OUTLAYS IS SOMEWHAT LARGER FOR THE CAPITAL (OR DEVELOPMENT) ACCOUNT THAN FOR THE RECURRENT ACCOUNT IN FY 1967 AND THE CAPITAL ACCOUNT IS PROJECTED TO INCREASE EVEN MORE RAPIDLY IN FY 1968. GENERALLY SPEAKING, RECURRENT EXPENDITURE USUALLY REACHES BUDGETED LEVELS WHILE CAPITAL EXPENDITURE FALL SHORT. THIS WILL PROBABLY BE THE CASE IN FY 1968 AS THE PROJECTED EXPENDITURE FOR CAPITAL ACCOUNT IS EXTREMELY AMBITIOUS GIVEN PREVIOUS GOVERNMENT PERFORMANCE. THE NEW GOVERNMENT, HOWEVER, TURNED IN A BETTER PERFORMANCE IN FY 1967 THAN PREVIOUS GOVERNMENTS; CAPITAL BUDGET OUTLAYS FELL SHORT OF BUDGETED LEVEL BY ONLY 5 PERCENT OR ETH\$13 MILLION. TOTAL EXPENDITURES EXCEEDED THE ORIGINAL BUDGET BY APPROXIMATELY ETH\$115 MILLION WITH THE INCREASE GOING PRIMARILY FOR HIGHER SALARY COSTS AND DEFENSE EXPENDITURES.

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3. WITH RESPECT TO FUNDING, THE MOST IMPORTANT DEVELOPMENT SINCE THE EPMG ASSUMED CONTROL IS THE INCREASED USE OF LOCAL

RESOURCES. THE MOST IMPORTANT COMPONENT OF THIS INCREASE IS THE RAPID BUILD-UP IN DEFICIT FINANCE. SINCE THE PREVIOUS GOVERNMENT USED THIS TECHNIQUE ONLY TO A LIMITED DEGREE, THERE IS SUBSTANTIAL ROOM FOR INCREASING GOVERNMENT DEBT OVER THE SHORT RUN. INFLATIONARY PRESSURES WILL, OF COURSE, BUILD UP AND INCREASES IN THE RATE OF INFLATION WILL DEPEND IN PART ON THE PRODUCTIVITY OF THE PROJECTS AND PROGRAMS WHICH THE GOVERNMENT FINANCES IN THIS MANNER, THE RATE OF MONITIZATION IN THE COUNTRYSIDE AND THE DESIRE OF PEOPLE TO HOLD CASH. THE FY 1968 BUDGET PROBABLY UNDERSTATES THE NEED FOR DEFICIT FINANCE AS SEVERAL POTENTIAL EXPENSES HAVE NOT BEEN COVERED IN THIS BUDGET (I.E., MILITARY PROCUREMENT, MAINTENANCE OF NATIONALIZED HOUSING, COMPENSATION FOR NATIONALIZED BUSINESSES AND LAND) AND A SUPPLEMENTAL BUDGET LATER THIS FISCAL YEAR WILL BE REQUIRED. THE OTHER ITEM SHOWING A MAJOR INCREASE IS NON-TAX REVENUE WHICH IS COMPOSED MAINLY OF RENTS FROM NATIONALIZED PROPERTIES AND PROFITS FROM NATIONALIZED BUSINESS ENTERPRISES. THIS LIMITED OFFICIAL USE

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FIGURE, WHILE HIGH, IS PROBABLY REASONABLE AS IT APPEARS TO BE BASED ON GROSS INCOME IN THE CASE OF RENTS (I.E., NO ALLOWANCES FOR DEPRECIATION OR MAINTENANCE). PERHAPS THE MOST SURPRISING ASPECT OF FY 1967 REVENUE PERFORMANCE IS THE SMALL (9 PERCENT) INCREASE IN TAX YIELD. FROM EARLIER REPORTS IT WAS GENERALLY ASSUMED THAT TAX REVENUE WOULD BE UP SUBSTANTIALY AS A RESULT OF IMPROVED COMPLIANCE; INCOME TAX PAYMENTS DID INCREASE 25 PERCENT FROM FY 1966 TO FY 1967, A VERY CREDITABLE PERFORMANCE, BUT EXPORT AND PROPERTY TAX COLLECTIONS LAGGED DURING FY 1967.

4. WHILE THE INCREASE IN ETHIOPIAN SOURCE FUNDS IS DRAMATIC IN ABSOLUTE TERMS, AS A PROPORTION OF THE TOTAL EXPENDITURE THEY DECLINED FROM 81 PERCENT IN FY 1966 TO 78 PERCENT IN FY 1968. THE INCREASE IN EXTERNAL SOURCE FINANCING IS 30 PERCENT FROM FY 1966 TO FY 1967 AND 57 PERCENT FROM FY 1967 TO FY 1968. ALMOST ALL OF THIS INCREASE IS IN LOANS BUT AS ETHIOPIA'S EXTERNAL DEBT IS NOT - SO FAR - VERY BURDENSOME (THE DEBT SERVICE RATIO FOR FY 1967 WAS 7.8) THIS FINANCING STRATEGY CAN BE USED OVER THE NEXT FEW YEARS WITH RELATIVELY LITTLE RISK TO ITS DEBT SERVICE CAPACITY.

5. TABLE B BELOW SETS FORTH THE ALLOCATION OF EXPENDITURES BY BROAD FUNCTION. IT SHOULD BE NOTED THAT LOANS AND CREDITS HAVE BEEN DISTRIBUTED AMONG THE FUNCTIONAL CATEGORIES IN THE CAPITAL ACCOUNT LINE ITEMS. GRANTS COULD NOT BE DISTRIBUTED BY FUNCTIONAL CATEGORY BUT ARE INCLUDED AS ITEM V AND BROKEN INTO RECURRENT AND CAPITAL ACCOUNTS.

TABLE B
BUDGET BY FUNCTION

(US FISCAL YEARS - MILLIONS OF ETHIOPIAN DOLLARS)

	1974	1975	1976	CHANGE	CHANGE
	(ACTUAL)	(PROV)	(BUDGET)	75/74	76/75
I. GENERAL					
SERVICES	263	362	377	38	4
A.RECURRENT	263	361	376	37	4
B.CAPITAL	-	1	1	-	-
II. ECONOMIC					
SERVICES	166	232	415	40	79
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A.RECURRENT	60	65	91	8	40
B. CAPITAL	106	167	324	58	94
III. SOCIAL					
SERVICES	175	233	319	33	37
A.RECURRENT	147	201	268	37	33
B. CAPITAL	28	32	51	14	59
IV. OTHER					
(RECURRENT ONLY)	59	112	129	90	15
V. TECHNICAL					
ASSISTANCE	98	96	101	-2	5
A.ALLOCATED TO					
RECURRENT EXP-					
ENSES	66	64	45	-3	-30
B.ALLOCATED TO					
CAPITAL EXPENSES	32	32	56	-	75
VI.TOTAL	762	1035	1341	36	30
A.RECURRENT	530	739	864	39	17
B. CAPITAL	134	200	376	49	88
C. TECHNICAL					
ASSISTANCE	98	96	101	-2	5

6. THE NEW REGIME'S STRESS ON ECONOMIC DEVELOPMENT STANDS OUT IN TABLE B. ECONOMIC SERVICES ARE TO INCREASE BY 150 PERCENT FROM FY 1966 TO FY 1968, WITH THE CAPITAL COMPONENT PROJECTED TO INCREASE BY OVER 200 PERCENT. THIS IS A REFLECTION OF THE HIGH LEVEL OF INVESTMENT FUNDS (75 PERCENT OF TOTAL FOR FY '68) ALLOCATED TO THIS SECTOR. AGRICULTURE AND ROAD CONSTRUCTION GET THE LION'S SHARE OF OUTLAYS IN THIS FIELD. IN SOCIAL SERVICES THE SHARPER INCREASE IS PROJECTED TO BE IN RECURRENT EXPENDITURE PROBABLY BECAUSE OF INCREASED EXPENDITURE FOR SALARIES OF TEACHERS, HEALTH WORKERS, LAND REFORM CADRE, AND SO FORTH. THESE INCREASES WILL PRESUMABLY BE FOR SALARIES FOR NEW EMPLOYEES, AS NO GENERAL SALARY INCREASE IS CURRENTLY PLANNED.

7. ANOTHER WAY OF MEASURING THE PRIORITIES OF THE NEW GOVERNMENT IS BY EXAMINING THE PROPORTION OF THE BUDGET (CALCULATIONS EXCLUDE GRANT TECHNICAL ASSISTANCE BECAUSE DISTRIBUTION AMONG FUNCTIONS IS NOT AVAILABLE) ALLOCATED TO EACH FUNCTION. IN FY

1966 GENERAL SERVICES COMPRISED 40 PERCENT OF THE TOTAL, ECONOMIC SERVICES 25 PERCENT, SOCIAL SERVICES 27 PERCENT AND OTHER 9 PERCENT. IN FY 1967 THE PERCENTAGES WERE GENERAL SERVICES LIMITED OFFICIAL USE

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39 PERCENT, ECONOMIC 25 PERCENT, SOCIAL 25 PERCENT AND OTHER 12 PERCENT WHILE IN FY 1968 THEY ARE BUDGETED TO BE GENERAL SERVICES 30 PERCENT, ECONOMIC 33 PERCENT, SOCIA 26 PERCENT AND OTHER 10 PERCENT. THE NEW REGIME TOOK OVER ABOUT MID-YEAR FY 1967 AND IN SPITE OF HEAVY INCREASES IN SALARIES AND DEFENSE EXPENDITURE MANAGED TO MAINTAIN THE SAME PROPORTIONS AMONG FUNCTIONS AS IN FY 1966. FOR FY 1968 THE BUDGET CALLS FOR A SUBSTANTIAL INCREASE IN THE PROPORTION TO ECONOMIC ACTIVITIES WHILE THE SAHRE GOING TO GENERAL SERVICES IS TO DECLINE. THIS SEEMS UNLIKELY, HOWEVER, AS A SUPPLEMENTAL BUDGET WILL ALMOST CERTAINLY BE REQUIRED TO COVER DEFENSE PROCUREMENT AND WILL RESULT IN AN INCREASED SHARE FOR GENERAL SERVICES EXPENSES DURING FY 1968. THIS DOES NOT MEAN, OF COURSE, THAT EXPENDITURE FOR ECONOMIC DEVELOPMENT WILL BE SHIFTED TO GENERAL SERVICES; RATHER, AN INCREASE IN DEFICIT FINANCE TO COVER HIGHER OUTLAYS FOR GENERAL SERVICES IS MORE LIKELY.
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